



F E D E R A L
STUDENT AID

We Help Put America Through School

**FISCAL YEAR 2003
ANNUAL PERFORMANCE
REPORT**

November 12, 2003

Dear Customers and Stakeholders,

I am pleased to present the Fiscal Year (FY) 2003 Annual Performance Report for the Office of Federal Student Aid (FSA), Department of Education. I am also extremely pleased to report that FSA has earned its second consecutive unqualified opinion on its audited financial statements, achieving one of FSA's top priorities. Additionally, this year, FSA met the Office of Management and Budget's (OMB) mandated accelerated time frame for FY 2004 year-end reporting, a year earlier than required. This clearly demonstrates that FSA has established a firm foundation for financial management excellence as a result of the Secretary's focus on the President's Management Agenda initiatives and the issues that have historically caused the federal student aid programs to remain on the General Accounting Office (GAO) High-Risk List. Unqualified audit opinions in FY 2002 and again in FY 2003, coupled with the elimination of the longstanding financial management material weakness in FY 2003, is clear-cut evidence of sustained exceptional financial management performance by FSA.

I must thank the many people within FSA and across the Department for their hard work, dedication, and collaboration to improve our systems, programs, processes, and procedures so that we could attain this significant goal.

This is my second year as Chief Operating Officer (COO) and the second year that FSA has received an unqualified ("clean") opinion. In FY 2003, I worked closely with the FSA senior management team and staff, and others across the Department, to ensure that we continued to build on efforts begun in FY 2002 to maintain an unqualified opinion. FSA's structured planning and performance reporting process for this year aligned FSA's priorities with the strategic drivers of our work and enabled us to identify opportunities to improve and more clearly demonstrate the manner in which FSA meets its primary statutory responsibilities to:

- Improve service to students and other participants in the student financial assistance programs.
- Reduce the costs of administering the programs.
- Improve and integrate the information and delivery systems that support the programs.
- Ensure program integrity.

We have prioritized our FY 2004 project efforts with the important mandates of the Performance-Based Organization (PBO) as guiding principles. Our goals of maintaining an unqualified financial statement audit opinion and of permanent removal of the federal student aid programs from the General Accounting Office High-Risk List are first, closely followed by our continued efforts to integrate our remaining legacy systems and migrate them to newer technology solutions, as appropriate.

Critical projects to improve customer service, Integration, and program integrity for FY 2004 include:

- Continuing to strengthen and align our processes and procedures to support our new financial management system.
- Improving program compliance, monitoring, and integrity by continued implementation of an enterprise data vision, strategy, plan, and framework, to ensure data consistency, quality, and integrity across our systems and for providing our customers with easy access to the data they need.
- Ensuring that FSA's workforce is adequately prepared to meet future challenges and accomplish our important mission.

The accomplishments identified in this report, and our focused plans for the future, clearly demonstrate our commitment to deliver the right aid, to the right people, at the right time. FSA is dedicated to providing seamless and superior service in our daily operations, and to our quest to provide better system solutions and better business processes that have significant impact on ensuring program integrity, providing better customer service, and reducing the cost of program administration. I am continuing to hold myself, and every FSA staff member, to the highest performance and accountability standards in carrying out our mission.

As required by the Reports Consolidation Act of 2000, I assert that the financial and performance information contained in this report is complete and reliable. Based on our own internal evaluations and that of the independent auditor's report, FSA does not have any material deficiencies to report for FY 2003. FSA is in compliance with all requirements of the Federal Managers' Financial Integrity Act (FMFIA) of 1982, and FSA's financial management systems are in compliance with the Federal Financial Management Improvement Act (FFMIA) of 1996.

I look forward to working with all of you in the coming years as we continue to provide outstanding customer service, to integrate our systems, and to ensure the appropriate management and oversight of the federal student aid programs.

Sincerely,

Theresa S. Shaw

**FISCAL YEAR 2003
FEDERAL STUDENT AID
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Introduction

In 1998 Congress amended the HEA, creating a PBO for the delivery of federal student financial assistance. Since then, FSA has set out to address the four statutory goals for the PBO in its annual performance plans. Those goals are:

- Improve service to students and other participants in the federal student aid programs, including making the programs more understandable to students and their parents (Goal 1).
- Reduce the cost of administering the programs (Goal 2).
- Improve and integrate the information delivery systems that support programs (Goal 3).
- Develop an open, common, and integrated delivery system and information system for the programs (Goal 4).

Business Operations

FSA's mission is to help put America through school. Through federal grant and loan programs administered by FSA, millions of students who might not otherwise have access have been able to pursue a postsecondary education. The Federal Pell Grant, FFEL, Direct Loan, LEAP/SLEAP, and Campus-Based programs are the largest source of student aid in the United States, providing a total of approximately \$60 billion in new aid to nearly nine million postsecondary students in FY 2003. FSA's FY 2003 fiscal year high-level program volume statistics are provided in Part I, Management's Discussion and Analysis. In addition, a few key FY 2003 business operations statistics are provided below:

- Processed 13 million FAFSA forms for academic year 2003-2004.
- Processed nearly 26 million Direct Loan payments from borrowers.
- Handled nearly 36 million inbound and outbound customer service calls across all call centers.

FY 2003 Performance Plan

FSA's FY 2003 Annual Performance Plan was developed under the leadership of a new COO and involved the participation of all levels of staff within the organization. Under COO Terri Shaw, the organization developed and adopted five objectives consistent with the government-wide strategies and initiatives outlined in the President's Management Agenda, the Department of Education's Strategic Plan, and the issues responsible for the inclusion of the federal student aid programs on the GAO High-Risk List. Most important,

these objectives are also closely aligned to the four PBO statutory goals identified above. The objectives are:

- Integrate FSA systems and provide new technology solutions (aligned with Goal 1 and Goal 4).
- Improve program integrity (aligned with Goal 2 and Goal 3).
- Reduce program administration costs (aligned with Goal 3).
- Improve human capital management (supports all goals).
- Improve products and services to provide better customer service (aligned with Goal 1).

The development of the FY 2003 Annual Performance Plan identified 18 priority projects representing the entire organization's efforts to achieve the stated objectives. The projects were also specifically weighted for urgency and value to assure that they were important to 1) the business of providing aid to applicants; 2) getting an unqualified opinion on the financial statements; and/or 3) getting the FSA programs off of GAO's High-Risk List. The priority projects are listed in Exhibit A, along with their end-of-year completion status.

HIGHLIGHTS OF FSA'S FY 2003 PERFORMANCE

During FY 2003, FSA improved products and services and achieved concrete results in integration and program integrity. At the same time, while maintaining FY 2002 operating budget levels, the organization improved its human capital management to meet tomorrow's federal aid delivery needs. Highlights of the most important results and outcomes are discussed below by objective.

OBJECTIVE ONE – INTEGRATE FSA SYSTEMS AND PROVIDE NEW TECHNOLOGY SOLUTIONS

FSA is continuing to provide appropriate and integrated technology solutions that enable the delivery of federal student aid in an efficient and cost-effective manner. We have developed and are executing a multi-year plan to integrate and improve our systems. Projects in the FY 2003 Performance Plan deliver visible and direct results for students, schools, and financial partners. Our e-commerce strategy is aimed at reducing the cost of delivery of financial aid to each student by making our business process faster, less error-prone, and less labor intensive, while at the same time improving the quality of service to customers. FSA accomplished the goals it set out to achieve. Of these, the most notable include the following.

Enterprise Data Strategy

In FY 2003, FSA committed to delivering an overall approach for streamlining and integrating systems to ensure that accurate and consistent data are exchanged between our customers, partners, and compliance/oversight organizations. The purpose of the Enterprise Data Strategy is to define FSA's enterprise data vision and plan for how it will combine the tools, techniques, and processes to manage its enterprise data needs. It will address the following data concerns: 1) business flow of data across the enterprise; 2) data structure and architecture; 3) primary ownership; 4) standards; 5) management and governance; 6) access methods; and 7) quality and integrity. This strategy is fundamental to our future technology investments.

Specifically, the strategy focuses on consolidating the various data strategy components—including technical strategies, student and institution common identifier strategies, access and enrollment management, and the XML strategy—into a comprehensive strategic vision. The target state of the strategy has three main components: 1) business process changes; 2) common data architecture; and 3) a technology strategy that supports the integration of processes and data to provide an enterprise solution for FSA.

The strategy will include high-level implementation and sequencing plans, which will define the order and alignment of those systems that require re-engineering and business process integration. In addition, the strategy will help deliver improved quality and service to customers and enable better management decisions, creating a more responsive and cost-efficient organization.

Although the strategy and high-level implementation plan were not final until November 2003, many important major milestones were met that are noteworthy to this report. Documents that were completed include:

- Data-centric view of the “As-Is” FSA system Data Flows.
- A Data Quality Report that highlights the high-priority data quality issues.

- Technical Strategies recommendations for Web Services, Internal and External Data Exchange, and Data Storage and Access Management solutions needed to support the future needs of the organization.
- XML Strategic Assessment and Enterprise Vision and XML Core Component Dictionaries that are included in the Department's overall Data Architecture.
- High level design for the Single Student Identification Method.
- Routing Identification (RID) options analysis to allow FSA to identify and associate Trading Partner Institutions with other related entities.
- Enrollment and Access management objectives and high-level requirements for reducing/managing multiple user ID's and passwords.

Recipient Financial Management System (RFMS) and Direct Loan Origination System (DL0S)

Implemented in April 2002, the COD system became operational, integrating the origination and disbursement processes for two of FSA's largest student financial aid programs, Pell Grants and Direct Loans. The processing systems that handled processing before COD were RFMS and DL0S. Those systems were not retired immediately after COD began processing due to the differences between the Pell Grant and the Direct Loan programs, their relative complexity, and the fact that for the first time two \$10 billion programs would be processed on the same platform. To mitigate potential risk, these system retirements and associated timeframes were planned as part of the COD contract management and development process. Accomplishing this project means that FSA has gone from two systems to one system for processing its largest two programs, which together account for almost half the program funding administered by the Department.

Lender Application Process (LAP) and Lender Reporting System (LaRS)

The LAP system, which became operational last fiscal year, allows prospective lenders and servicers to request enrollment in the FFEL Program and provides online verification and updating of demographic data for existing FFEL Program lenders and servicers. The LaRS, which became operational this year, automates the Interest and Special Allowance Request (Formerly ED Form 799) and supports an electronic integrated business application for managing the lender payment process. LAP/LaRS was designed and developed last year to support a centralized, controllable, and consistent accounting process for lender payment management. Prior to the development of these systems, thousands of lenders requested payments through an inefficient paper-driven, front-end process. These new systems directly contribute to erroneous payment risk reduction and meet government mandates for electronic processing of payments. The stabilization of the LAP/LaRS system that was performed in FY 2003 included operational support, data validation, change request management, and the design, development, testing, and implementation of application fixes, changes, and enhancements.

Form 2000

The Form 2000 project, known as the Guaranty Agency Financial Report (GAFR) was originally implemented in October 2000. Since the initial implementation, the Guaranty Agency (GA) community and the FSA users, developers, and operators have identified and requested a number of enhancements to the system. The 2003 GAFR enhancements include system functionality that allows monthly, quarterly, and annual GAFR submissions, additional soft and hard edits to help ensure data consistency, the ability for GA's to create amended annual entries, and the creation of a custom conversion and interface to transfer annual GAFR transaction data to the FSA subledger in order to create annual report journal entries. These enhancements will give GA's more control over data submission, improve data accuracy, and improve audit trails and internal controls by providing and supporting increased financial oversight of default collection activities, reimbursement claims, and portfolio status.

eZ-Audit

eZ-Audit is a new Web-based application that provides schools a single point of submission for financial statements and compliance audits to the Department. The school simply signs on to eZ-Audit, enters summary audit and financial data into a Web form, attaches an electronic version of its report, and clicks the submit button. eZ-Audit strengthens internal management controls through the electronic submission, storage, and secure access of compliance audits and financial statements. The electronic data capture minimizes processing errors, reduces paper, and eliminates lost documents. The automated workflow decreases backlogs, shortens cycle times, and helps to balance resources.

Common Services for Borrowers (CSB)

FSA took significant steps to implement the integration of its borrower back-end support systems and business processes. In an effort to improve loan portfolio management, FSA conducted market research, listened to industry professionals, took a commercial approach, and decided to combine borrower-related functions into an integrated process known as CSB.

In FY 2003, FSA initiated a competitive procurement for CSB to incorporate our three major loan servicing systems and customer service functions (including the Direct Loan Servicing System, the Debt Collection Management System, and the Direct Loan Consolidation System) into a more efficient, cost effective, and customer-centric model. This procurement was conducted using a two-phase source selection procedure, in accordance with applicable federal procurement laws and regulations and FSA's procurement flexibility statute (20 U.S.C. 1018a(d)).

It has been determined that CSB will improve FSA's loan portfolio management and yield significant cost savings, significant customer service improvements, and significant business process improvements. The vision to improve the management of student aid

obligations owned by the Government will be accomplished by streamlining the current contract systems and operations under a single contract. This re-engineering effort will drive operational efficiencies, reduce unit cost, and improve customer satisfaction through integrated business processes. The scheduled contract award is in November 2003.

Debt Management and Collection System (DMCS)

The current DMCS environment comprises a 13-year old mainframe system, 72 interfaces, and over 15 stand-alone sub-systems. The objective of the DMCS re-engineering project is to modernize the existing collection processes to be more aligned with the commercial sector and to replace the existing collection systems with a leading edge debt recovery management solution. This will strengthen FSA's ability to manage the collections portfolio. The DMCS re-engineering project was incorporated into the Common Services for Borrowers solicitation.

Electronic PLUS Master Promissory Note

The electronic PLUS Master Promissory Note (MPN) project was undertaken to provide an electronic option for parents borrowing through the Direct Loan Program. FSA now offers an electronic multi-year promissory note alternative for all three sub-programs of the Direct Loan Program. A Web-based electronic MPN option was developed in 2001 for subsidized and unsubsidized Direct Loans made to student borrowers. This supplemental implementation extends that capability to parent borrowers.

OBJECTIVE TWO – IMPROVE PROGRAM INTEGRITY

FSA is continually working to improve program integrity. It is committed to demonstrating that it is aggressively managing the federal student aid programs in a manner that ensures access to postsecondary education while reducing vulnerability to fraud, waste, and abuse. We made great improvements in demonstrating sound financial management by strengthening our internal controls and financial management systems, including supporting processes and procedures, so that reliable and timely information is available to manage FSA's day-to-day business operations. Our program integrity efforts continue to be aimed at maintaining a balanced approach to minimize noncompliance and default rates, while still promoting the widespread use of the programs. Specific accomplishments follow.

Unqualified Audit Opinion

FSA accomplished one of its priority goals and received an unqualified opinion on its FY 2002 financial statements. An unqualified opinion had not been received in several years. In addition, the FY 2002 Internal Control Report identified only one material weakness and noted improvements. FSA's commitment to demonstrating sound financial management is its top priority. The Department successfully deployed the Joint Financial Management Improvement Project compliant Oracle Federal Financials in January 2002. In FY 2003 many important enhancements were completed. The new system offers real-time information coupled with the ability to produce timely financial statements. The Secretary's management improvement initiative continues to focus high-level attention on FSA's remaining management improvement initiatives. These actions represent significant progress toward the Department's objectives for improved financial management, reporting, accountability, and an unqualified opinion. In preparation for FY 2004 accelerated year-end reporting, the Department is further refining its audit preparation plans and tightening its closing process.

GAO High-Risk List

FSA faces a management challenge as it provides billions of dollars of grants and loans through thousands of intermediaries to millions of students who may not yet have established credit. Since 1990, GAO has reported on government programs and functions that it has identified as "high-risk" because of their greater vulnerabilities to fraud, waste, abuse, and mismanagement. GAO designated the federal student aid programs as high-risk in its initial report, and it has continued to give the programs this designation. A primary management goal of the Secretary is to remove FSA's programs from GAO's list of high-risk programs. The Secretary and the COO are committed to the permanent removal of the FSA programs from this list and to demonstrating that FSA is effectively managing the inherent risks of the programs. The receipt of the unqualified opinion on the FY 2002 financial statement audit was a critical accomplishment towards this goal, although it was not received in time to be considered by GAO prior to its January 2003 designation of the FSA programs as high-risk.

In May 2003, Secretary Rod Paige made a formal request to GAO for a mid-cycle reconsideration of the high-risk designation based on demonstrable progress made in addressing the issues that had caused the FSA programs to be designated as high-risk. On June 9, 2003, GAO denied the Secretary's request, primarily because at the time of the designation GAO did not have sufficient evidence of the Department sustaining financial management improvement. In responding to GAO in July 2003, the Secretary, though disappointed, recognized that by working toward this goal the Department continues to build a foundation for management excellence that will benefit it and its programs for many years. Improvements have been made in financial management and in the strategic management of human capital. In addition, better management of IT resources is improving services for customers and partners, and FSA is modernizing to improve program integrity.

FSA will continue to follow GAO's guidance document, *Determining Performance and Accountability Challenges and High Risks* (GAO-01-159SP), to address the issues raised by GAO in the high-risk designation. In FY 2003, FSA accomplished key activities that were aimed at addressing these issues, and we continued to use them as a priority as we finalized our FY 2004 Annual Performance Plan. We are committed to working with GAO staff to ensure that they are informed of our progress toward resolving Department management issues and sustaining improvement in the FSA programs so that a positive assessment will be received in the GAO High-Risk Update Report, scheduled to be issued in January 2005.

Internal Controls

In addition to obtaining an unqualified opinion, FSA made significant improvement over internal controls. Effective internal controls are essential to programmatic and financial stewardship and accountability in order to prevent waste, fraud, and abuse. In FY 2003, FSA was able to:

- Reduce reconciliation time for all FSA operating partner activity to FMS (FSA ledger) and to FMSS (Department's general ledger) to within 30 days of month-end close.
- Review all accounting treatment to ensure compliance with standard general ledger accounting.
- Develop account validation framework for system development and ongoing certification of accounting and program systems providing financial data.
- Develop the framework for measuring whether the accounting validation is successful by performing independent post-production.
- Develop trial balance capability for FSA operating partners to facilitate and expedite the reconciliation process.
- Strengthen FSA's financial reporting to ensure full compliance with OMB Circular A-124, Management Accountability and Control, and Credit Reform.
- Better prepare and review quarterly and annual financial statements.

- Remind schools of the requirement to complete verification of selected students for Pell Grant and Direct Loan disbursement data after the COD program was implemented.
- Improve the monitoring mechanism to reduce the occurrence of prior material weaknesses and reportable conditions.

Reconciliation Operational Procedures

In order to identify improvements and fill gaps in the procedures related to reconciliation, FSA School Delivery Services staff collaborated with the COD Customer Service Representatives, systems contractors, CFO/FMS, and OCFO GAPS staff continually throughout FY 2003. This collaborative work led to several system releases and hundreds of incremental improvements made during daily and weekly conference calls. As a result, processing, reconciliation, and year-end closeout were easier for both schools and FSA.

Default Management and Prevention Strategies

In July 2003, a new function for portfolio risk management within Borrowers Services became operational. The unit, the Portfolio Risk Management Group, was created to provide an organizational focus to better support a fully integrated approach and provide designated resources to student loan default management and prevention strategy management. This new unit formalizes the FSA focus on mitigating loss in the loan programs.

In FY 2002, the Department identified strategies for default management and prevention activities to: 1) improve default prevention, 2) improve recipient and school eligibility, and 3) improve default collection. During this fiscal year, the Portfolio Risk Management Group worked with other FSA Service representatives to conduct an even more comprehensive inventory analysis of the existing default prevention activities across the organization, identifying and validating FSA-wide default prevention strategy areas. This group also identified the three top-risk attributes for default:

- The borrower did not complete the program of study.
- A correct telephone number for the borrower was not available.
- The borrower could not be contacted for 12 months (360 days delinquent prior to transfer to FSA's Debt Collection Service).

FSA's debt strategy is one that emphasizes mitigating risk through portfolio management and appropriate use of tools for default prevention. In FY 2003, due diligence efforts were implemented that have a focus on effectiveness; they include increasing contact efforts for high-balance delinquent accounts. Outreach efforts such as conferences with guaranty agencies, lenders, and schools to share best practices in this area, and debt management partnership with the National Council of Higher Education Loan Programs continue to demonstrate that default prevention is a high priority for FSA.

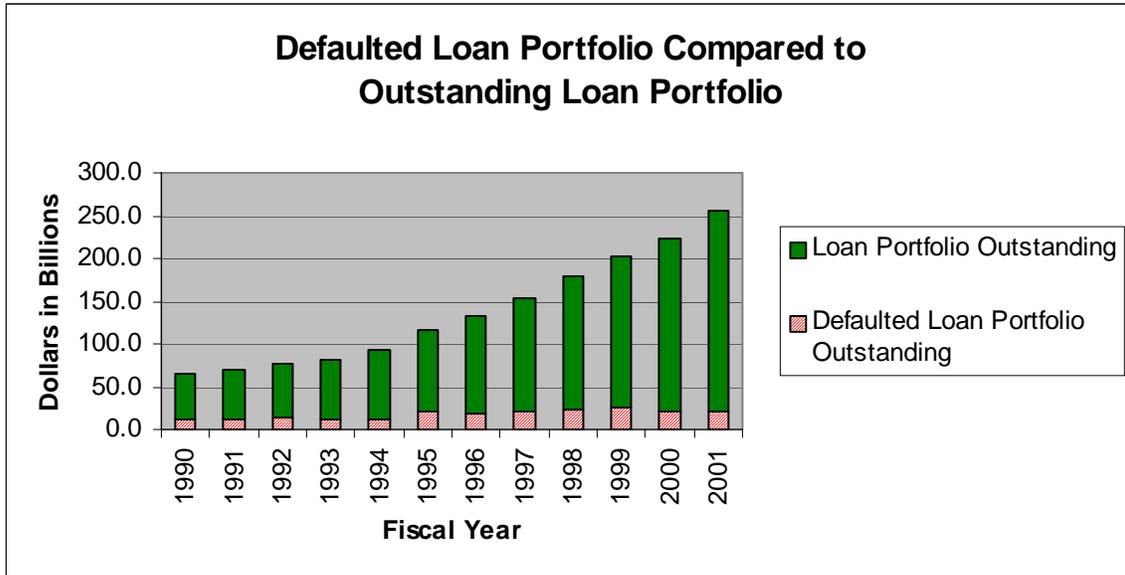
An additional accomplishment in this area was the Late Stage Delinquency Assistance Program, an initiative that was implemented this year to mitigate potential default in the Direct Loan Program. The purpose of the program is to elicit assistance from schools in locating and contacting borrowers prior to the borrower going into default. Initial results are promising.

Default Collections

FSA has continued to effectively manage the default portfolio, which is shown by FSA's ability to exceed the FY 2003 collections goal. The FSA default portfolio was \$13.975 billion at the beginning of FY 2003. During FY 2003, default collections, excluding consolidations, totaled nearly \$1.33 billion. The result was a recovery rate of 9.5 percent, far above the FY 2003 goal of 7.6 percent. In addition to realizing a record year for combined recoveries on debts owed by individuals, FSA saw higher collections by private collection agencies this year than in previous years. Total default recoveries, including recoveries by the GA's, exceeded \$5 billion in FY 2003 for the third year in a row. Over \$350 million has been collected by matching the entire defaulted loan portfolio with the National Directory of New Hires, a database that contains employment and income information on all persons employed in the United States. This enables the Department to find current addresses for more than two million defaulters. Other achievements in default recovery include:

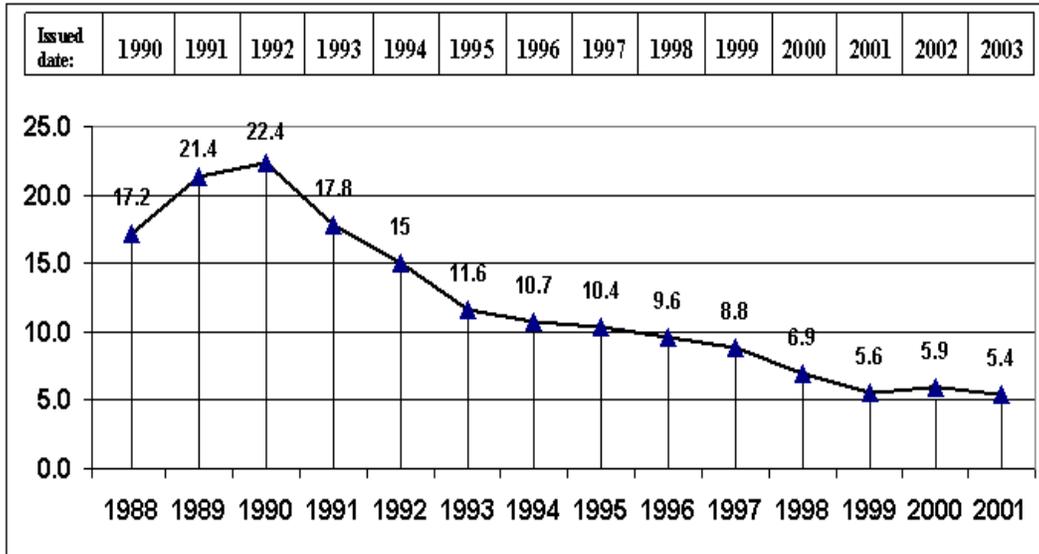
- \$700 million through federal income tax refunds and other federal offsets.
- \$470 million through wage garnishment of defaulters.
- \$2 billion by consolidating defaulted loans.
- \$900 million gained through loan rehabilitation.
- \$980 million through regular collection.

The following chart is an indication of our continued success in this area. As the value of the FFEL and Direct Loan portfolio has risen, the percent attributed to the defaulted portfolio has dropped.



Cohort Default Rate (CDR)

The CDR, a major indicator of our accomplishments under our default management and prevention strategies, continues to decrease. It reached an all-time low of 5.4 percent for the FY 2001 rate, which represents the most current data available. The FY 2001 cohort default rate is a snapshot in time of borrowers who began repaying their loans between October 1, 2000 and September 30, 2001 and who defaulted before September 30, 2002. In addition, for the first time ever, all schools have rates low enough to ensure they remain eligible for federal financial aid programs. (In the last decade, nearly 1,200 schools have lost eligibility to participate in the federal loan programs due to their high default rates.) Credit for this accomplishment is shared with the financial aid community, which improved its efforts to counsel borrowers and to inform them of the numerous flexible repayment options designed to meet individual repayment needs. Also, the 1998 Amendments to the HEA extended by three months—from 180 days to 270 days—the length of time it takes a delinquent borrower to default on a student loan. The effect of this change was first felt with the release of the FY 1998 cohort default rates, which decreased by 1.9% from the FY 1997 rates, with approximately half of the decrease being attributed to the time extension. For the last three years, with the release of the FY 1999, 2000, and 2001 rates, the change in default date has been fully implemented. As the chart below demonstrates, the national cohort default rate has dropped nearly every year since 1990, when it peaked at 22.4 percent.



Oversight and Compliance Measures

FSA has been criticized by GAO and the Inspector General (IG) for not being able to demonstrate it has a balanced management approach to school oversight and compliance. In order to address this issue, FSA developed measures to demonstrate the effectiveness of FSA’s monitoring strategy. The measures include:

- Monitoring of institutions and program dollars.
- Monitoring of overall compliance.
- Managing risk.
- Providing technical assistance to schools new to the FSA Programs.

In FY 2003, 2,544 schools (40 percent of all schools participating in the FSA Programs) were monitored through a comprehensive review. These schools comprise 40 percent of all program dollars. Four percent of all schools received an on-site program review, and one percent of schools received an on-site compliance improvement visit. In FY 2003, the total number of schools having a risk probability greater than 80 percent in FSA’s school risk assessment system was 558, or 9 percent of all schools participating in the FSA programs. In addition, the total funding of schools having a risk probability greater than 80 percent equaled nearly \$2.3 billion, or 4 percent of all program dollars. In future years, FSA will trend this type of information, as well as the recently developed oversight and compliance measures, to demonstrate the effectiveness of FSA’s monitoring strategy or to identify where improvements can be made.

Financial Partners Data Mart

The first two releases of the Financial Partners Data Mart created a central repository to accomplish the following functions: risk management, customer relationship management,

compliance management, and portfolio management. This year's release of the Data Mart, which is its third phase, enables FSA to assess program risk areas, evaluates FFEL participation through a risk model or scorecard, and raises efficiencies in the lender and guaranty agency oversight and monitoring process. The new enhancements also provide access to lenders, allowing them to have access to only their designated information and to a select list of reports.

Guaranty Agency and Lender/Servicer Risk Management Guides

FSA developed new interim guaranty agency and lender/servicer program review guides in an effort to continue to enhance oversight and improve consistency and risk management. This was done in partnership with the financial aid community. As a result, FSA is now able to obtain more information to use in review planning prior to going on-site, including electronically submitted documents from the entities. As a result, reviewers are able to analyze and determine areas of risk or concern much earlier than before. Because these guides were developed with input from the financial aid community, the establishment of clear expectations concerning the review scope and process has resulted in a more effective work environment with the organization being reviewed.

Overall FSA Security and Privacy Architecture

A major challenge in developing security and privacy architecture is determining the proper level and means of authentication to provide a safe and secure environment for borrowers, schools, and financial partners to conduct their transactions. For FY 2003, the goal was to define an overall vision to guide planning and development of FSA security and privacy technical services and components. Implementing an enterprise security architecture for FSA will ensure that systems are developed and maintained in accordance with Federal requirements and will employ controls that ensure the public trust.

OBJECTIVE THREE – REDUCE PROGRAM ADMINISTRATION COSTS

As FSA continues to receive level-funded operating budgets, the reduction of program administration costs is one of the most challenging objectives before us. FSA is focused on linking performance to budget decisions and improving performance tracking and management. Ultimately, the goal is to further improve control over resources and to maintain greater accountability for their results. Although in FY 2003 other priorities kept FSA from measuring our costs to determine whether we were progressing towards our statutory goal of reducing administrative costs, this was still an important driving strategy as we identified the activities for our FY 2003 Annual Plan. A few activities that supported this objective in FY 2003 follow.

Budget and Contracts

In recent years FSA has been able to maintain a relatively flat operating budget while supporting continued increases in program volume and workload, so that it could make IT investments. FSA's ability to manage and control operating expenses is based on a philosophy of good fiscal management and continual process improvement to increase productivity and operational efficiencies, coupled with innovation in our products, services, and supporting technologies. In FY 2003, FSA developed and implemented processes and procedures to better manage how it initiates, renews, and extends contracts. These processes and procedures are designed to help ensure that FSA receives the highest value service for the lowest possible cost.

Executive Dashboard

Cost management is being accomplished by establishing a set of metrics to measure performance and productivity trends across the enterprise over time. These metrics will guide improvement initiatives that optimize the return on investment and reduce costs. In FY 2003, FSA developed the Executive Dashboard, which provides management a weekly view of operational metrics, budget, contracts productivity, and performance metrics at the aggregate and service delivery level. The Dashboard is shared across the organization on a weekly basis so that all FSA employees can measure the progress they are making as an organization toward their objectives and goals.

Electronic Products and Processes

In recent years FSA has converted several paper processes and services into electronic formats, which result in savings. The results of these processes and services for FY 2003 are as follows:

- Nearly 7.7 million *FAFSA on the Web* applications were processed in FY 2003, compared to 5.8 million last year. This represents a 33 percent increase in electronic processing of student aid applications.

- COD processed approximately 30 million records for approximately six million student borrowers and grant recipients in its first year of operation (as of April 29, 2003).
- 1-800-4-FED-AID, the Federal Student Aid Information Center, received over 7 million calls this year. Service levels have increased with 99 percent of calls completed, a 3.1 percentage point increase over last year, and the average speed to answer reduced by 66.1 percent to nine seconds.
- As of September 30, 2003, there were 602,036 Direct Loan borrowers enrolled in Electronic Debit Account (EDA), an increase from its first year of 54,884 borrowers in FY 1999. The federal government has saved over six million dollars since the inception of the EDA program.
- In August 2003, FSA implemented a new cost saving process to receive electronic change of address records from the U.S. Postal Service rather than through paper postcards. Direct Loan Servicing receives an average of 1.5 million postcards annually. At a cost of \$0.70 per post card, FSA pays the Post Office up to \$21,000 per month. The new electronic postcards will reduce costs by approximately 70 percent.

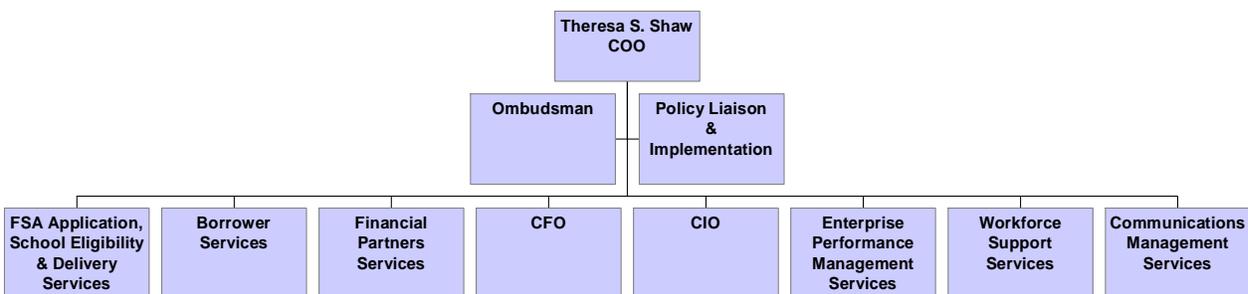
OBJECTIVE FOUR – IMPROVE HUMAN CAPITAL MANAGEMENT

FSA has made substantial progress in building, sustaining, and effectively deploying a skilled, knowledgeable, diverse, and high-performing workforce that is aligned with FSA’s objectives. In addition, FSA employees have worked on several One-ED and other human capital improvement projects that the Department has prioritized in the Strategic Plan to address the President’s Management Agenda Human Capital Management Initiative. A few key human capital management accomplishments in FY 2003 follow.

Reorganization

The COO proposed a new functional organization structure for FSA that is aligned with FSA’s strategic drivers, business objectives, and operational goals. This new organization structure was approved by the Department and implemented on July 13, 2003.

FSA ORGANIZATION STRUCTURE



Under the new structure, FSA is an organization:

- In which people are empowered to get things done.
- That fosters and expects continual innovation and learning.
- That is fluid and readily adaptable to business changes.
- That attracts and retains top talent for employment.
- In which the inherent risks of the programs are effectively managed.

Succession Planning

FSA recognizes the importance of developing succession-planning options that produce excellent leadership teams and ensure continuity of exceptional management. In 2001, GAO identified strategic human capital management as a government-wide challenge and in April 2002 GAO specifically recommended that FSA implement a succession plan (*Federal Student Aid: Additional Management Improvements Would Clarify Strategic Direction and Enhance Accountability GAO-02-255*). In conjunction with the Office of Management, FSA Workforce Support Services conducted an analysis of its vulnerability

due to the retirement of key officials. Through this effort, Administration and Workforce Support Services identified 241 employees who are or will become eligible for retirement before the end of calendar year 2006. Working closely with FSA management, Administration and Workforce Support Services determined that 169 of those employees were in key positions that, if vacated, could disrupt FSA's ability to accomplish its mission. To ensure minimal disruption, they identified 117 employees with the qualifications to fill behind these key positions, and they developed a strategy for filling behind the remaining 52 positions. That strategy includes, but is not limited to, detail assignments to temporarily fill behind the retiring employees until the positions can be recruited for and filled permanently.

Employee Training

FSA continued to provide employees with the support and training opportunities necessary to achieve its mission. Training courses such as *Solution Life Cycle Development*, *COD*, *Introduction to Enterprise Application*, and *System Security* provided staff an overview of the technologies used in the modernization of FSA. Training sessions entitled *Leadership Excellence* were delivered to all FSA managers to further the development of strong leaders in FSA who will lead the organization in meeting its performance objectives. Specific attention was paid to collaborating for results and performance management.

OBJECTIVE FIVE – IMPROVE PRODUCTS AND SERVICES TO PROVIDE BETTER CUSTOMER SERVICE

Customer Satisfaction Surveys

This year FSA resumed use of the American Customer Satisfaction Index (ACSI) survey methodology to measure the customer satisfaction of FSA's most high profile, frequently used products and services. The ACSI uses a widely accepted methodology to obtain standardized customer satisfaction information; it is used by 180 companies in 29 industries representing about 75 percent of the nation's economy. The products and services that were surveyed were *FAFSA on the Web*, Direct Loan Servicing, COD, and LaRS. The results follow.

FSA PRODUCT OR SERVICE	ACSI SCORE
FAFSA on the Web	86
Direct Loan Servicing	77
COD	66
LaRS	71

The National ACSI benchmark for the private sector is 74, and the Federal Government benchmark is 70. The *FAFSA on the Web* score is exceptional and approaches Amazon.com's score of 88, which is ACSI's highest score ever obtained. Both *FAFSA on the Web* and Direct Loan Servicing, the only two components for which prior satisfaction information is available, showed an improvement of three points and eight points, respectively, from their 2001 ACSI scores. Scores for LaRS and COD are lower but are in line with business-to-business satisfaction results, which range from 65-74 for banking and telecommunications firms.

Electronic Products

In FY 2003, FSA improved and employed greater usage of currently available electronic products:

- The eZ-Audit was introduced in April 2003 allowing schools to submit their financial statements and compliance audit data online. This Web-based application benefits schools because the forms are pre-populated with demographic information on the school, and there is automatic error checking prior to a submission, instant acknowledgement of receipt after submission, no copying and mailing costs, and 24/7 access to their reports and electronic data.
- Beginning this year with the release of the FY 2001 CDRs, FSA transmits CDR notification packages to schools electronically via the Student Aid Internet Gateway (SAIG). This electronic process replaces the paper notification process for all Title IV schools located within the United States.

- Based on feedback from institutions participating in the federal student aid programs, FSA began an initiative to move more PC-based software to the Web. Development is nearly complete on two Web products, and testing will begin in October 2003.
- In March 2003, FSA launched “FSA for Counselors,” an online student aid resource for middle school, secondary school, and TRIO counselors. Features include the High School Counselor’s Handbook, federal student aid publications, videoconferences, and scripts and slides for presenting a financial aid night.
- In July 2003, a Dear Colleague Letter was posted to the Information for Financial Aid Professionals (IFAP) Web site announcing the new MPN for the Federal Perkins Loan Program. The Perkins MPN is designed as a multi-year, multi-loan promissory note for students. Generally, as long as the student and the school do not change, a new note is not required. This MPN is optional for the 2003-2004 school year and will become mandatory beginning November 2004.
- In July 2003, Direct Loan Consolidation received the first Electronic Verification Certifications (EVC) from lenders. They are used in the purchase of federally insured student loans for Direct Loan Consolidation. The new Web-based EVC allows lenders to log on to a secured Web site and either complete EVC’s online or download and upload a batch file to collect EVC data from their loan-holder systems.
- Finally, the Government Paperwork Elimination Act requirement to provide the public an electronic alternative to all paper transactions has been virtually completed.

President’s Management Agenda e-Gov Initiatives

The goal of FSA’s participation in the e-Gov initiatives is to make it easier for borrowers and partners to receive high quality service by expanding the federal government’s effective use of electronic technologies. This includes support of IT projects that offer performance gains across agency boundaries, such as eLoans and students.gov. Another example of an e-Gov initiative is GovBenefits, whose goal is to reach out to the public and ensure they know about available programs within the Department and across the government. The result of this initiative is higher visibility of programs to those citizens who could use the assistance. The FSA team performed a substantial amount of work in FY 2003 to increase the number accessible via the Web site. At the beginning of FY 2003, the Department had 23 programs on the Web site, and now there are 64 education programs on the GovBenefits.gov Web site. In addition, FSA assists the Department as the managing partner for the eLoans initiative and manages the cross-agency Web portal, students.gov.

OMBUDSMAN'S REPORT

The FSA Student Loan Ombudsman works directly with student loan borrowers, loan holders, and schools in an informal dispute resolution process. The range of complaints, from simple questions to complex long-term problems, can inform future FSA activity as well as changes to the student aid programs overall. Issues resulting from the complaints are summarized and shared both internally and externally and are considered when addressing the need for systemic changes. The office heard from 17,664 complainants in FY 2003, an approximate 6 percent increase over the 16,707 for FY 2002. Of those, 3,621 required intense research and facilitation of outcomes on longstanding issues, an approximate 9 percent increase from the 3,305 in FY 2002.

The bulk of the Ombudsman activity involves disputes in which an Ombudsman specialist works with the borrower, loan holder, schools, and other parties to gather facts, establish a common understanding of the problem, and work toward resolution. Cases involve all loan and school types. It often takes 60-90 days to thoroughly research the underlying issues on these cases.

For the first three years of operations (FY 2000-FY 2002) the most prevalent category was "Account Balance." In FY 2003, "Loan Cancellation/Discharge" dominated the research questions. The top five case issues, in order of frequency, were:

- Loan Cancellation/Discharge (e.g., dispute ineligibility).
- Account Balance (e.g., too high, incorrect).
- Repayment Plans/Amounts (e.g., needs more options).
- Consolidation (e.g., borrower wants to consolidate).
- Default (e.g., cannot make payments).

Issues are tracked to inform FSA leadership and loan holders so that corrective action can be taken to prevent similar situations and so that the potential for program change can be evaluated.

New for FY 2003 was sharing the case information with the Customer Service Review Board that FSA put into place to review what FSA customers are telling us at all levels. The long-term results should be fewer Ombudsman cases as the Board works to address the systemic issues raised.

Effectiveness of the case activity is measured through customer comment and through an OMB-approved weekly survey. Borrowers whose cases closed recently are chosen at random and asked to respond to questions on Ombudsman service accessibility, knowledge of representatives, timeliness of resolution, level of satisfaction with resolution, and overall Ombudsman service. On a scale of 1-5, where 1 is the *highest* possible rating, the FY 2003 rating from customers with single-issue questions was 1.81. The higher rating of

1.50 was for the research cases that take more time to resolve and involve more direct customer contact.

LEGISLATIVE RECOMMENDATIONS

The Department of Education continues to believe that routine data matches with the IRS would strengthen the financial integrity of the student aid programs. FSA, OPE, and legislative affairs offices are collaborating with staff from OMB and Treasury, as they work with congressional committees (to date the Joint Committee on Taxation and House Ways & Means) on proposed legislative language that would amend the Internal Revenue Code to accomplish this objective. The matches would allow the verification of applicant income information submitted on the student aid form (the FAFSA) with information from official income tax records.

FSA will continue to make suggestions and offer advice on any legislative recommendations the Administration prepares for reauthorization of the HEA.

POSITIONING FOR THE FUTURE

FSA has drafted its FY 2004-2008 Five-Year Plan, supported by an Integrated Business and System Sequencing Plan that contains the details of our projects and initiatives. The draft Five-Year Plan establishes tactical goals for achieving each of our strategic objectives, which were once again validated by FSA senior leadership in the FY 2004 planning process. We believe that the plan will provide useful information to our stakeholders and Congress that can be used to hold us accountable and measure our progress. This plan will be provided to the community for comment in the first quarter of FY 2004. It highlights the projects FSA has undertaken, or will undertake, that deliver the most visible and direct impact for students, schools, and financial partners. Our goal to transform FSA systems is reiterated in the plan—to make FSA technology processes Web-enabled, and our systems integrated and consolidated. The Enterprise Data Strategy continues to be the cornerstone of the plan to support an integrated, simplified business and technical model that will allow students, schools, and financial partners to access the information they need, when they need it—on paper, by telephone, and over the Internet—in a secure manner that addresses appropriate privacy concerns.

For FY 2004, the following work priorities remain for FSA: 1) continuing to run our operations to ensure students are provided the funds to support their higher education; 2) sustaining our financial management improvements; 3) addressing the issues to remove the student aid programs from the GAO High-Risk List; 4) integrating the remaining legacy systems and their ultimate migration to newer technology solutions; and 5) developing and implementing workforce alignment initiatives to support FSA performance goals and the

Department's One-ED objectives. In addition, an important FY 2004 priority will be to better measure and report on our administrative costs to determine whether we are progressing towards our goal of reduced administrative costs in our business processes. FSA's success in implementing these action items will directly contribute to greater employee productivity, accountability, and morale, better operational systems, increased program integrity, reduced program costs, and—ultimately—improved products and services for our customers.

FSA is committed to providing access to postsecondary education by providing the right money, to the right people, at the right time, and at the right cost. The results of this year's Performance Plan are proof of that commitment. There were many successes in FY 2003. Based on these successes, 19 bonuses were awarded to the COO and the senior managers in FSA. A bonus of \$72,500 was awarded to the COO. Eighteen bonuses were awarded to other senior managers of FSA. These awards ranged from \$33,844 (23.75 percent of annual salary) to \$3,756 (4.38 percent of annual salary), with a median award of \$12,540 (11.13 percent of annual salary).

We intend to continuously identify issues and develop solutions in support of our mission to help put America through school. We are confident that with the availability of sufficient resources our efforts will result in improvements in all aspects of our operations and services.

Exhibit A
PERFORMANCE PLAN STATUS AT A GLANCE
As of September 30, 2003

FSA No.	Indicator	Final Status
1	Obtain an unqualified ("clean") opinion on FSA's financial statements	✓
2 *	Develop and execute an FY 2003 plan for removal from the GAO High-Risk List	✓
3	Reconcile FSA accounts to Department's general ledger within 30 days after month-end close by 9/30/03	✓
4	Implement the proper accounting structure and appropriate internal controls in all systems impacted by FSA's system integration and technology solution initiatives	✓
5	Develop trial balance capability for each operating partner (ACS, Raytheon, EDS, COD) to facilitate and expedite the reconciliation process	✓
6	Address material weaknesses and reportable conditions in audits	✓
7	Implement Form 2000 enhancements needed since original deployment in October 2000	✓
8	Determine the scope of the Debt Management Collection System (DMCS) re-engineering	✓
9	Improve school's fund management, reconciliation, and closeout processes	✓
10	Stabilize the Lender Application Process (LAP) and Lender Reporting System (LaRS)	✓
11	Enhance Program Monitoring and Oversight	✓
12	Develop and standardize an integrated contract management approach that utilizes performance measures that are directly linked to the business case objectives	Continued in FY 2004
13	Create an Enterprise-level dashboard of productivity and performance metrics	✓
14	Develop and/or implement workforce alignment (business processes, skills, etc.) initiatives and actions to support FSA performance goals and One-ED objectives	Continued in FY 2004
15	Implement integrated project management oversight for FSA's system integration initiatives	✓
16	Define an enterprise-wide data strategy and high-level implementation approach that addresses the business flow of data across the enterprise, architecture, primary ownership, standards, management, access methods, and quality	Continued in FY 2004
17	Analyze Personal Identification Number (PIN) issues related to enterprise wide management/architecture strategy	✓
18	Create an overall FSA integrated security and privacy architecture	✓

Key:



Completed

*

Performance project completed but project success measure not met.